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**Sweden's Admission to NATO,  
and its Macroeconomic Consequences**

**By**

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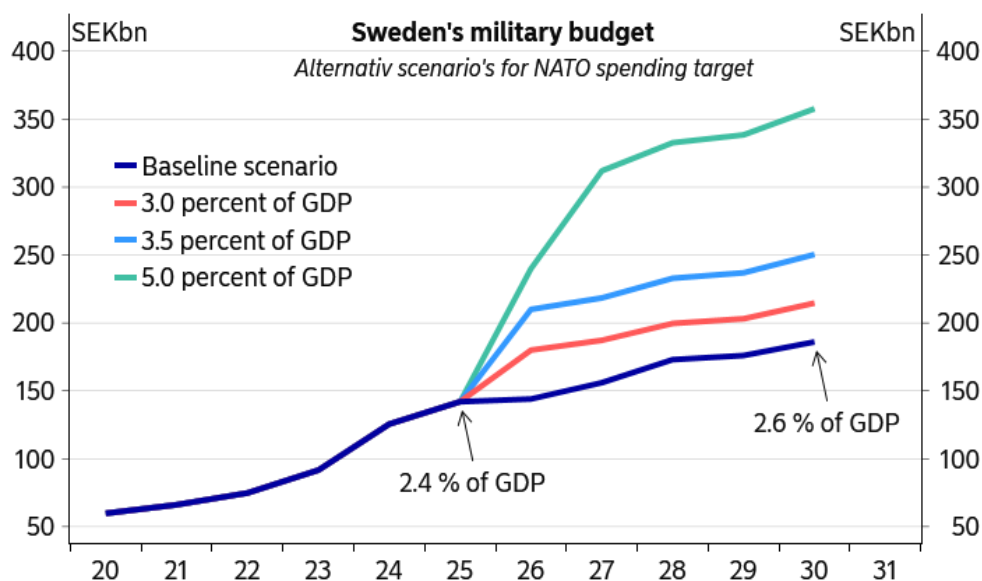
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### Executive Summary

- ✦ Following the invasion of Ukraine in Russia in 2022, Sweden decided to break its decades long policy of neutrality and join NATO, thus adding to the mounting pressure on the Russian Federation since Finland joined in 2023. Despite this pressure, the risk of military escalation remains limited.
- ✦ Sweden has not lost time in increasing its defence spending to an estimated 2.4% in 2025, double the level of 2020. The shock brought by the Russian invasion of Ukraine has pushed this country to change its decades-old prudent stance on fiscal policy - forecasted to go from a surplus to a balanced budget to boost defence spending.
- ✦ NATO membership decreases the geopolitical risk of an invasion of Sweden and thus a lower risk-premium for investing in the country and a lower risk of capital flights.
- ✦ Recent calls by President Trump for allies to spend up to 5% of GDP have raised concerns about the cost of that protection. In response, Sweden plans to raise defence spending to 3.5% of GDP by 2030, backed by SEK 300 billion in loan-financed investments and a fast-tracked procurement strategy through 2028.
- ✦ For an open economy such as Sweden the tariffs set by President Trump, which seem to be correlated with the defence spending of EU countries, represent a significant challenge, and threaten to hit the country's \$17 billion worth of export to the US. Sweden faces risks from tariffs—especially on metals and vehicles—which could impact up to 0.8% of its GDP.
- ✦ It is reasonable to assume the increased defense spending would be financed by increasing the Swedish debt- to-GDP ratio. However, in the long-term relying on an increasing structural deficit is not a viable solution, hence significant shifts in the composition of the national budget might be necessary.
- ✦ The Swedish government could redistribute significant resources from welfare to defence spending. This might change public support for NATO membership.
- ✦ Sweden and Finland's NATO membership boosts the alliance's Arctic presence, but rather than fueling militarization, it should be used to strengthen stability and crisis management through renewed cooperation in forums like the Arctic Council.
- ✦ A revival of the sense of national identity might be necessary to convince the general public that certain sacrifices are necessary for the sake of National security, however this phenomenon at the same time risks increasing sympathies for far-right parties.

### Key Picture: Sweden's Projected Military Budget (Scenario's for NATO Spending Target)



Source: Nordea, Macrobond and Government Offices of Sweden, from [Corporate Nordea](#). \* Baseline scenario refers to government's decisions to 2025 according to current plans, thereafter proposals. Last updated 20 February 2025

## 1. Introduction

Russia's 2022 invasion of Ukraine marked a turning point in European security, prompting Sweden to abandon its long-standing policy of neutrality and apply for NATO membership. With Finland joining the alliance in 2023, NATO has gained two of Europe's most advanced economies and extended its direct border with Russia by over 1,300 kilometers. The accession of Sweden and Finland not only strengthens NATO's technological and economic base, but also increases strategic pressure on Moscow at a time of growing regional instability.

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Sweden's accession to NATO marks the end of over two centuries of armed neutrality—a policy born in 1812 after a devastating loss to Russia, and one that kept the country out of both World Wars, the Cold War, and every major European conflict since 1814. For generations, neutrality was not just a strategic posture but a core element of Sweden's international identity: promoting diplomacy, multilateralism, and non-alignment in a deeply divided world.

Even during the Cold War, as Soviet troops occupied Central Europe and tensions ran high, Sweden remained officially neutral—choosing stability and independence over formal alliance commitments, while quietly maintaining defense cooperation with the West. That legacy has now been set aside. Russia's 2022 invasion of Ukraine is widely cited as the catalyst for Sweden's decision to join NATO, yet the long-term implications of this choice remain open to question.

Senior Russian officials have already stated that from that moment Sweden would be regarded as a threat, while Finland warned Sweden of a probable increase in hostile operations against it carried out by the Russian Federation. However, even if the tone of the threats escalated even further, the risk of an actual military escalation remains limited: so far Russia has already shown to prefer non-military retaliatory measures, both for Sweden and Finland.

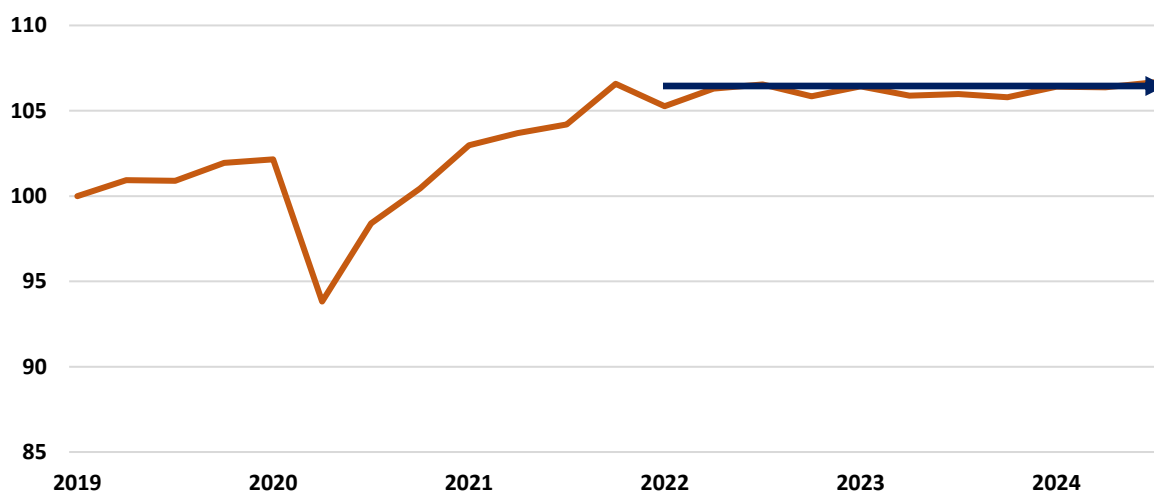
This was to be expected given that the Russian military is still engaged in a consuming conflict in Ukraine, and most likely lacks the resources to open another front, especially since a military escalation with what is now an official member of NATO might trigger article 5 of the North Atlantic Treaty.

However, even if President Trump is unlikely to truly abandon NATO allies, regardless of his previous public statements on this matter, this does not mean that US protection will come without a price.

## 2. Macroeconomic Developments

Sweden's economy remains weak, with growth falling short of expectations, though signs of recovery have begun to emerge. 2024 marked another disappointing year for the Swedish economy, with only marginal GDP growth and a rise in unemployment (**Figure 1**). Economic momentum remained weak heading into the new year.

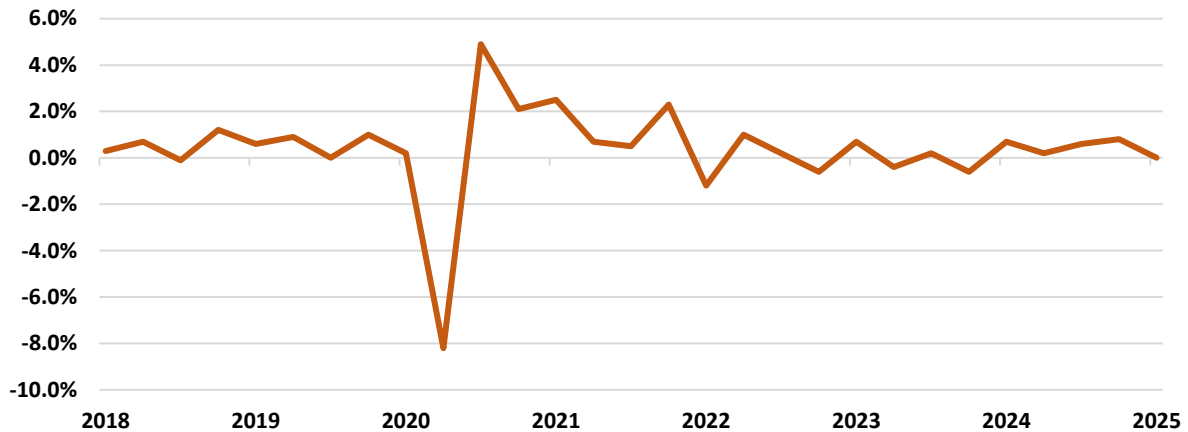
**Figure 1: The Recovery In Growth Has Been Delayed (Index 2019=100)**



Source: Fred

In Q1 2025, GDP growth stalled quarter-on-quarter, a notable deceleration from the marginal growth of 0.6% and 0.8% in Q3 and Q4 respectively (**Figure 2**). This marked the weakest performance since the contraction in the Q4-2023. Household spending remained flat, as increased purchases of food and beverages were offset by reduced outlays on restaurants and accommodation.

**Figure 2: Swedish Economy Recorded Sluggish Growth in 2024 and No Growth in 2025**



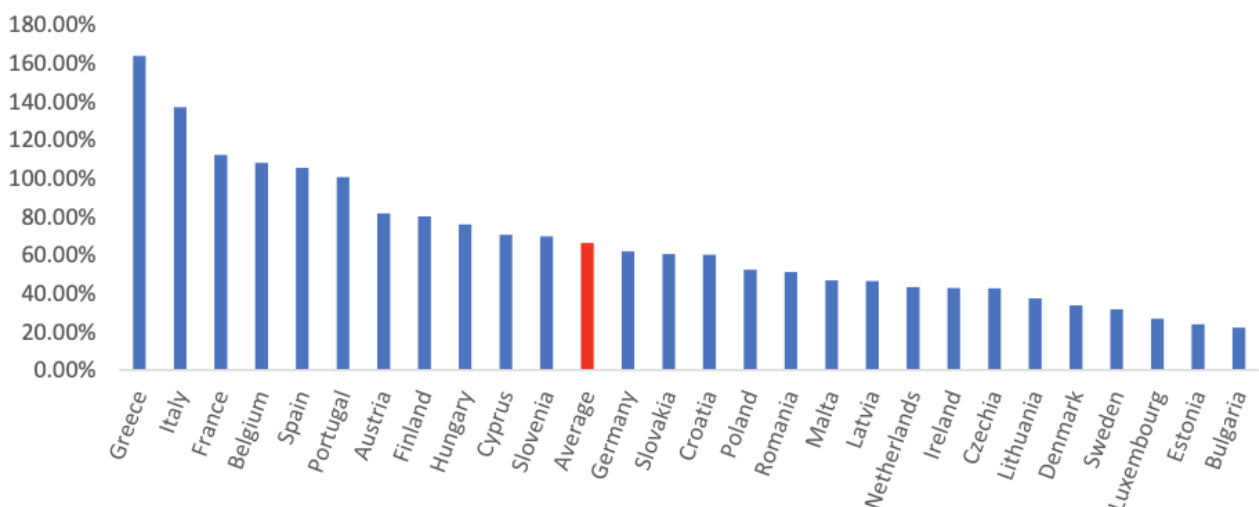
Source: Fred

After several tough years marked by inflation and high interest rates, Swedish households are beginning to recover. Housing prices have started to rise again—historically a strong signal of improving household demand—and consumer sentiment is turning more optimistic. Stabilised inflation and rising real incomes are expected to boost spending in 2025. Households have remained resilient, with debt levels stable and the debt-to-income ratio falling due to income growth. With financial buffers still intact, consumption is likely to accelerate gradually through 2025 and into 2026.

### 3. The Economic Effects of Greater Defence Expenditure

Sweden has not lost time in increasing its defence spending to an estimated 2.4% in 2025, double the level of 2020. The shock brought by the Russian invasion of Ukraine has pushed this country to change its decades-old hawkish stance on fiscal policy, as now Sweden is forecasted to go from a surplus to a balanced budget in order to boost defence spending (even if they went from a surplus to a deficit it would not be an issue given that Sweden's Debt-to-GDP ratio is around 30% as of today).

**Figure 3: Debt-to-GDP Ratio: EU Countries 2024 Q2**



Source: Eurostat Database

This kind of fiscal stimulus would prove beneficial in the short term for the Swedish economy, as it might help offset the lower growth caused by President Trump Tariffs. This is especially true since [Sweden has a world-class military-industrial complex](#), which means that an increase in Defence spending would benefit primarily the Swedish Economy.

Even if the entire amount was not spent on domestic production, given that the US are the major exporters of weapons at the global level, it stands to reason to assume at a EU-US deal to decrease tariffs might be [hinged on an increase in purchases of military equipment from the US](#), in this regard an increase in military spending can be seen as an investment both in local production and in international relationships.

Furthermore, NATO membership decreases the geopolitical risk of an invasion of Sweden, which in turn means a lower risk-premium requested for investing in the country and a lower risk of capital flights. NATO membership provides economic stability right when Sweden needs serious and stable investments, and the benefits of this outweighs the costs of the possible [hybrid-threats posed by Russia](#). However, while this may be true, NATO membership also exposes Sweden to the risks of being drawn into broader Russia–NATO confrontations—risks it could have avoided under a policy of armed neutrality.

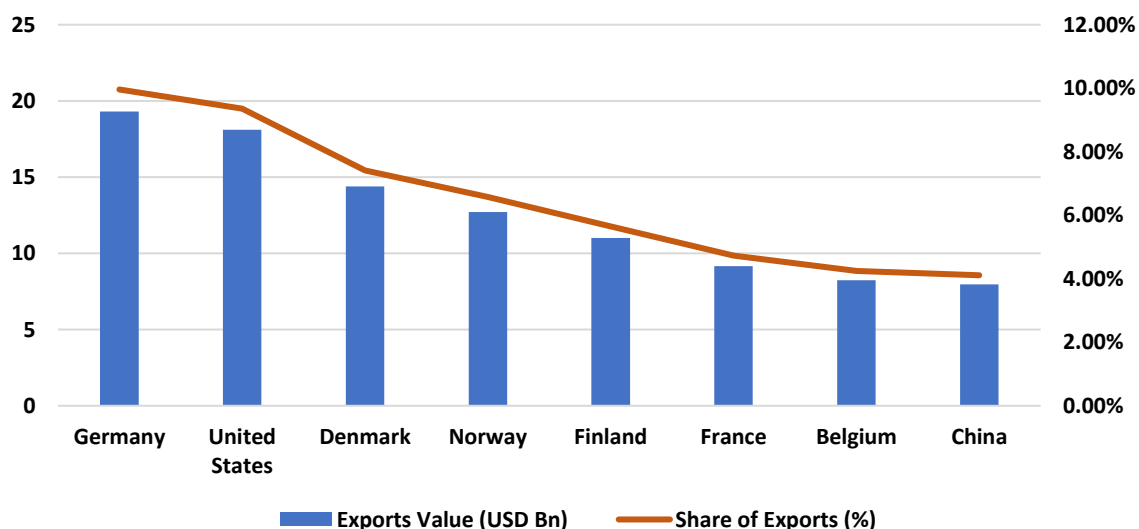
The costs incurred to respect NATO obligations would help to prevent much costlier wars on Swedish soil, not to mention that a secure [Baltic sea, now almost entirely surrounded by NATO countries, is vital for trade](#), which is in turn vital for Sweden.

While many assumed NATO membership would ensure protection under the U.S. security umbrella, recent calls by President Trump for allies to spend up to 5% raise questions about the reliability and cost of that protection. This is why Sweden plans to increase defence spending to approximately [3.5% of GDP by 2030](#). The strategy includes loan-financed investments totaling over SEK 300 billion (USD 30 billion) by 2034, with a phased transition to balanced funding starting in 2035. Under an agreement between the Government and the Sweden Democrats, an initial SEK 25 billion (USD 2.5 billion) will be allocated from 2025 for fast-track “opportunistic purchases” of critical materiel—such as air defence systems, drones, rocket artillery, protective gear, and ammunition—for delivery between 2026 and 2028.

#### 4. The Impact of Tariffs on Sweden

Sweden is a highly export-dependent economy, with exports accounting for [about 55% of GDP in 2024](#). The bulk of these are goods—primarily vehicles, machinery, pharmaceuticals, paper products, and iron and steel. While most exports go to Nordic and other European countries, the United States is Sweden’s third-largest individual export market.

**Figure 4: Export Destinations by Country**



Source: OEC World

For an open economy such as Sweden the tariffs set by President Trump, which seem to be correlated with the defence spending of EU countries, represent a significant challenge and threaten to hit the country's \$17 billion worth of export to the US. A potential risk for Sweden is US tariffs on steel and aluminium, which make up 3.5% of Swedish exports—around 0.1% of GDP. Tariffs on EU motor vehicles are also under discussion, with cars and light vehicles comprising 22% of Swedish exports to the US, or roughly 0.7% of GDP.

However, if the trade war between the EU and the US was to escalate further, it seems likely that the EU would focus on addressing the issues of its internal market, which is Sweden's main export market. Page | 7

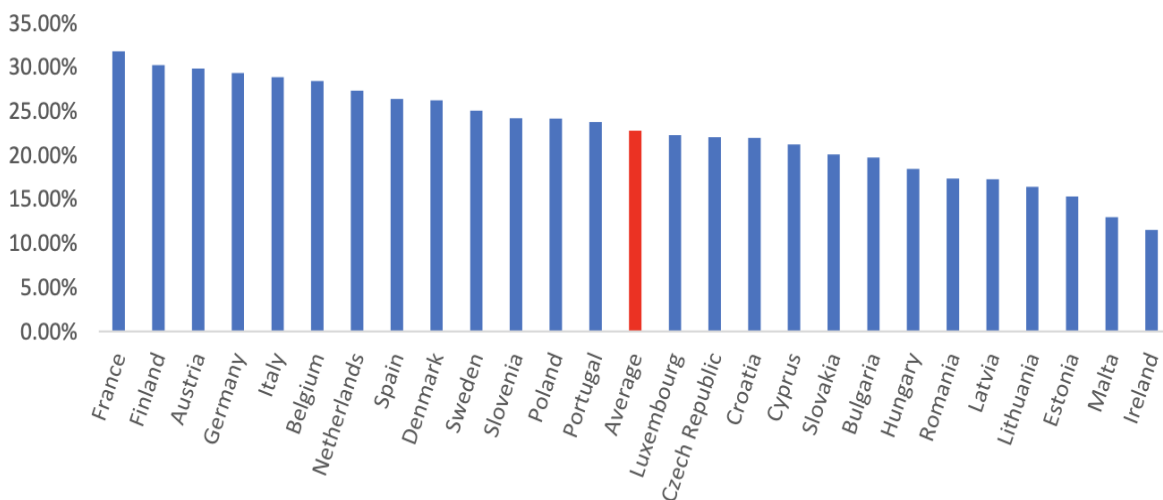
Hence, if the US and the EU were to find an agreement to end the trade war, as it seems the EU is interested to do, tariffs would be cancelled and trade between the two blocs might continue as before. If instead a solution was not found, the EU would have the incentives to solve the issues of its internal market to exploit its untapped potential for trade between EU countries, and that would give Sweden an alternative market for its domestic production.

### 5. Political and Social Consequences of the Crisis

So far, it was assumed that the increase in defence spending would be financed by increasing the Swedish debt-to-GDP ratio, that is a reasonable assumption both because this country currently shows rock-solid public finances and because the Swedish population, usually preferring fiscal prudence, does not seem to object the already forecasted increase in the national deficit.

However, in the long-term relying on an increasing structural deficit is not a viable solution, hence significant shifts in the composition of the national budget might be necessary if the current military build-up persists.

**Figure 5: Welfare State Expenses/GDP: EU Countries 2023 (except Greece)**



Source: Eurostat Database

Sweden is well renowned for its generous welfare state, which means that if the geopolitical tensions increased, and there was no end in sight for the war in Ukraine as the recent failure in the negotiations between the US and Russia has shown, the Swedish government could redistribute significant resources to defence spending.

As we can see from the graph above the average ratio between expenses related to the welfare state and GDP is on average above 20%, which shows that there is significant room for spending cuts should the so called “peace dividends” disappear, especially since “social protection represented the most important area of general government expenditure in 2022 for all the EU countries”.

The Swedish people have so far shown great support for NATO, as proven by the fact that there were no major protests following Sweden entry in the organization, despite the strong cultural and political leaning of this country for pacifism and neutrality; but if defence expenditure was to subtract resources from the generous Swedish welfare system this might change in the future.



Currently, there seems to be two main possible scenarios:

1. The geopolitical situation does not normalise in the short-medium term, the public support for higher defence spending remains high, even at the expense of lower social spending, as the real consequences of a war can be seen in Ukraine, [the risk of a Russian attack on a NATO country remains real, and the Swedish people are forced to choose the lesser evil.](#)
2. The risk of another war in Europe decreases as we manage to find a negotiated solution to the current crisis, and this allows trade with Russia to start again, as seems likely from [the significant appetite for trade shown by some western companies,](#) which would grant EU countries access to the much-needed large amounts of raw materials necessary for projects like the EU green deal and the revival of economic growth.

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In the first scenario the economy would be boosted by government spending in the defence sector, through a combination of higher structural deficit and lower social spending, and Sweden might also benefit from deeper integration between EU countries as these seek to exploit synergies between defence companies.

In the second scenario, defence spending declines, or stops increasing, as the threat of a war between Russia and NATO slowly decreases, and the Swedish economy benefits from higher levels of trade and higher economic growth at the EU level.

Which means that Sweden does not need to be afraid of a new “cold war” with Russia, especially since now it has NATO backing. At the same time, the Swedish population would rather live in the aforementioned second scenario, which shows that Sweden has a strong incentive to contribute to peace deals.

Conscription might be necessary to [hit the goal of 115.000 regular soldiers in the Swedish army by 2030,](#) a significant number if we remember that Swedish military build-up is a part of a wider effort coordinated at the EU level to increase conventional military forces.

Young swedes in particular seem ready to do their part for their country, with [only 10% of conscripts reportedly participating in compulsory military training against their will,](#) an impressive shift in public opinion if we consider that 15 years ago the number of new recruits began to shrank significantly due to the lack of support for the military.

Hence, the Swedish people seem ready to bear the burden of a higher defence spending and conscription for as long as necessary to deter an armed invasion of their country and their allies, but this does not mean that we should expect the current situation to persist forever.

## **6. NATO in the Arctic**

Sweden and Finland’s accession to NATO has extended the alliance’s footprint in the Arctic, enhancing its strategic position in a region shaped by climate change and geopolitical rivalry. [In March 2024,](#) over 20,000 troops from 13 NATO countries, including the U.S., Sweden, and Finland, joined Nordic Response exercises in Norway—part of a larger drill involving 90,000 troops, 50 naval vessels, and 100 aircraft.

While Russia has rebuilt many Soviet-era bases and maintains a sizable Arctic presence—including 40 icebreakers versus one for the U.S.—its posture remains largely defensive. Its military buildup centers on protecting the Northern Sea Route and logistical operations across a vast Arctic coastline. Despite alarm over “militarization,” Russia lacks the capacity for conventional land incursions into European Arctic territory.

NATO, meanwhile, retains superiority in nuclear submarine capabilities, especially now as the Arctic retains high on the US strategic agenda. Rather than escalating tensions, NATO should use Sweden and Finland’s membership to promote Arctic stability. Forums like the Arctic Council, though strained since Russia’s invasion of Ukraine, remain essential for communication and crisis management.



## 7. Immigration

A revival of the sense of national identity might be necessary to convince the general public that certain sacrifices are necessary for the sake of National security, however this phenomenon at the same time risks increasing sympathies for far-right parties, which have always represented themselves as the guardians of the cultural heritage of a country.

If support for these parties was to increase, as we are currently witnessing across Europe, that would most likely translate in much harsher immigration policies, on the same lines of the ones currently enacted by President Trump in the US.

Lower immigration levels would translate in a tighter job market and might increase the strain on national pension schemes as birth-rates keep on falling.

However, given that Swedish economic growth is founded on increasing productivity levels and strong investments in capital intensive industries the risk that its economy faces due to lower immigration levels is contained, hence in the short-medium term there does not seem to be any issue in that regard.

## 8. Conclusions

Sweden's entry into NATO reflects major shifts in the modern geopolitical landscape, however even as tensions rise the economic outlook for this country is not as bleak as it may seem: thanks to its solid fiscal situation Sweden has significant room to expand its debt-to-GDP ratio, and its somewhat resilient economy is well positioned to keep on growing regardless of whether the current military and commercial conflicts are solved or not. Furthermore, the Swedish people seem ready to do what it takes to protect their country, which means that the Swedish society will not hinder the necessary reforms, even if these reforms are likely to take a toll on the society itself.